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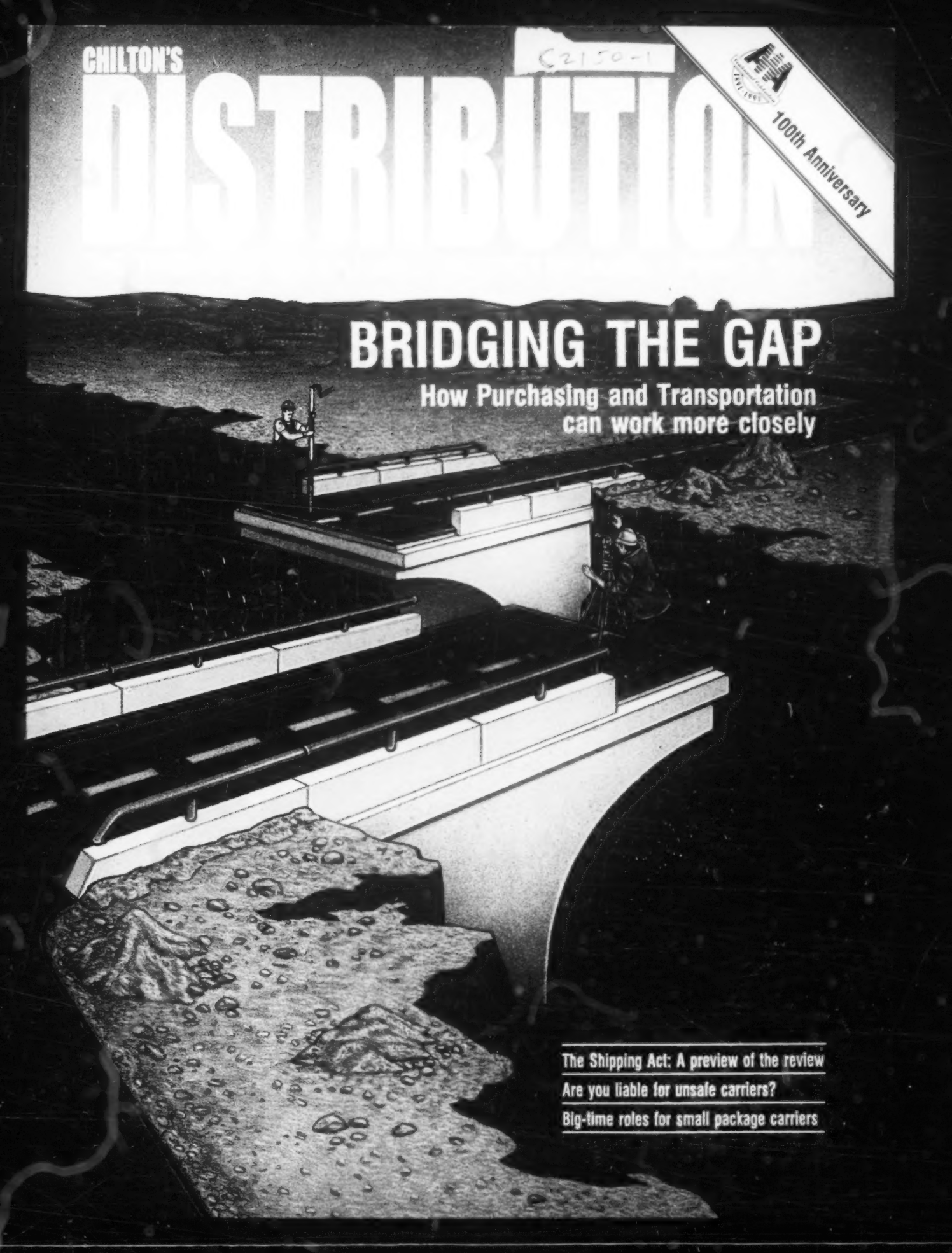
BRIDGING THE GAP

How Purchasing and Transportation can work more closely



The Shipping Act: A preview of the review

Are you liable for unsafe carriers?

Big-time roles for small package carriers

MARCH 1991

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COVER STORY

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Bridging the gap between purchasing and transportation can pay big dividends. Yet for many companies, the team effort required to hit the payoff remains elusive. The question is how to "cross-pollinate" the two disciplines so that each can take advantage of the other's expertise in order to make more cost-effective transportation purchasing decisions.

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How Much Information is Too Much?

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INBOUND BUYING HABITS DIE HARD

A new study shows that many companies now believe the best way to buy transportation is to integrate purchasing and transportation. Makes sense. The problem is, a lot of firms still haven't got the message.

By Jay Gordon, Executive Editor

Purchasing and transportation managers are slowly discovering that, together, they have the power to control inbound transportation cost and service.

For many—those that have traditionally left transportation decisions to the vendor—this comes as something of a revelation. Prior to the deregulation of truck transportation in 1980, freight rates were regulated, so it didn't matter whether you or your vendor arranged the transportation. You'd pay the same.

Today's purchasing and transportation managers, however, are free to negotiate deals with carriers that can yield substantial improvements in cost and service. The problem, however, is that old habits, and old misconceptions, die hard. For one reason or another, many of these professionals continue to forgo the opportunity to control inbound transportation.

That much is evident in the results of "Purchasing's Role in Transportation Decision Making," a new study from the Center for Advanced Purchasing Studies sponsored by DISTRIBUTION Magazine. The survey results can be broken down into three main areas:

• **Current purchasing practice.** For what percentage of transactions are companies controlling the inbound freight move? How does this percentage differ when total firm activity versus group or division activity are taken into consideration?

• **The level of purchasing's involvement in key decision making areas.** What transportation-related activities are purchasing managers actively involved in? What factors are important to purchasing in the selection of transportation modes and carriers?

• **The effects of organizational structure on transportation decision making.** Who has the responsibility for transportation decisions? Is there a connection between organizational structure and companies' ability to control inbound transportation? What organizational structure enables firms to make the best transportation decisions?

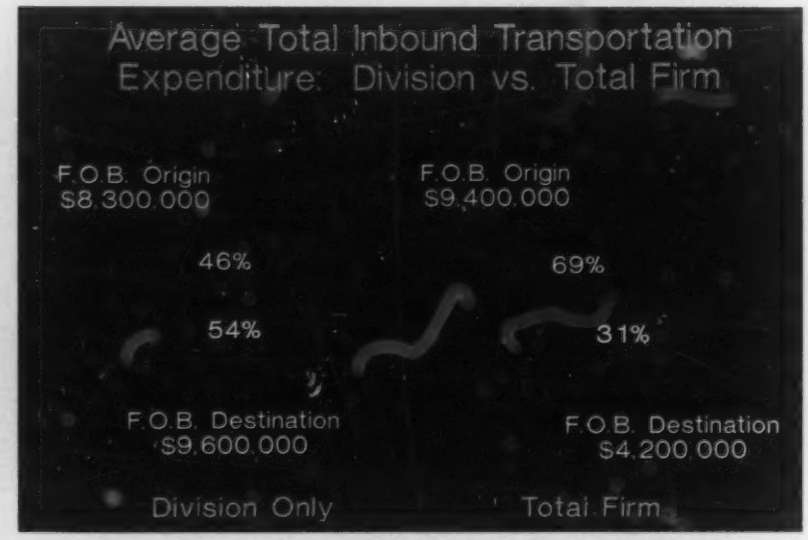

Fig. 1—Is there a lack of transportation know-how at the local level?

Current Purchasing Practice

Companies answering as a division or group only say they spend 46 percent of their annual inbound transportation dollars on freight that was shipped FOB-Origin—freight that they controlled. The other 54 percent of the freight was shipped FOB-Destination (Fig. 1).

For total firm responses, FOB-Origin terms covered 69 percent of the total annual inbound freight expense; the other 31 percent was FOB-Destination. When total firm and division/group responses are taken together, the breakdown is 57.5 percent FOB-Origin, 42.5 percent FOB-Destination.

A quick, if oversimplified, review may be in order. The term "FOB-Origin" implies that the buyer owns the goods in transit and is thus able to control their transportation. FOB-Destination means the seller owns the goods in transit and controls the transportation. While most of the

A CLOSER LOOK AT CAPS

An affiliation of the National Association of Purchasing Management and the College of Business at Arizona State University, CAPS provides advanced research on purchasing and materials management issues. "Purchasing's Role in Transportation Decision Making" represents CAPS' effort to redefine purchasing strategy in light of the dramatic changes in transportation since deregulation. DISTRIBUTION Magazine was a leading underwriter of this vital research effort.

"We feel it is important to identify trends that may reshape the future direction of purchasing with respect to overall company organization and strategy," says CAPS Director Dr. Harold E. Fearon. "In addition to assessing purchasing's role in transportation decisions, this research provides both purchasing and transportation professionals with a tool that will enable them to make better decisions in the future and increase their awareness of the changing operating environment." If you would like a free copy of the study "Purchasing's Role in Transportation Decision Making," please fill in number **603** on the Reader Service Card in the back of this issue.

firms responding to the CAPS study were able to report dollar amounts for inbound transportation, it is clear that the problem of identifying these costs cannot be overlooked. Determining what the firm spends on inbound freight is especially difficult when delivered pricing is used, since freight charges are simply rolled into the price of the goods.

These numbers can be interpreted in two ways. The fact that 57 percent of the firms use FOB-Origin terms indicates that the practice of buying goods based on a delivered price has become outmoded. Yet some 43 percent of the companies surveyed still use FOB-Destination terms. There are some legitimate reasons for this, but it is clear that a lot of companies have yet to get the religion on managing inbound freight.

It is interesting to note the difference in responses for entire firms versus division/group only. Respondents answering for the entire firm indicate a greater likelihood that their company will control inbound transportation. CAPS Research Associate Julie J. Gentry explains that there may be a lack of transportation expertise at the decentralized levels of these organizations.

Purchasing's Involvement

Purchasing managers are involved in a wide range of transportation-related activities (Fig. 2). In most cases, their level of involvement is increasing. Out of 10 transportation activities, the highest degree of involvement, naturally, was in inbound transportation (90 percent of responses). Other activities purchasing is involved in: choice of mode (88 percent), choice of carrier (85 percent), price determination (67 percent), rating carrier performance (67 percent) and outbound transportation (49 percent).

The high degree of purchasing involvement in key transportation areas indicates that many firms know the benefits of integrating transportation and purchasing expertise. Also, Gentry says, a high degree of involvement in rating carrier performance indicates that purchasing continues to be an integral part of the transportation process long after the carrier is chosen.

Service Ahead of Price

The most influential factor in determining the mode of transportation selected is the required delivery date, which received 37 percent of total possible ranking points. That was followed by the cost of transportation (17 percent), reliability and service quality (14 percent), shipment size (11 percent) and time in transit (10 percent).

On-time delivery topped the list of factors which influence carrier selection (25 percent of possible ranking points). Rates again was second (18 percent) followed by geographic coverage and time in transit (both 10 percent), shipment tracing and care in handling (both 6 percent), financial condition of the carrier (5 percent) and door-to-door deliveries (4 percent).

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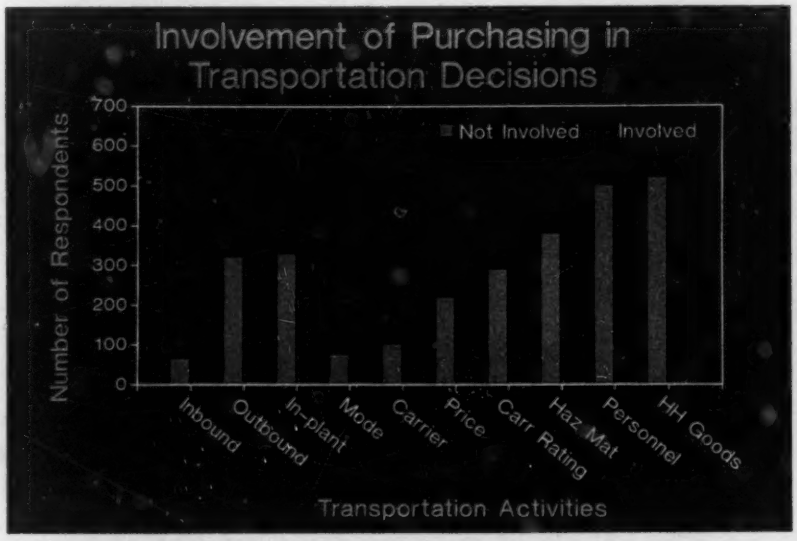

Fig. 2—Many firms know the benefits of integration.

SURVEY DEMOGRAPHICS

Data for CAPS' Transportation Purchasing Survey was gathered in the fall of 1990 from 678 U.S. companies covering 54 industry groups. Sixteen percent of these companies had 1989 sales of less than $10 million; 28 percent had sales of $10 million to $50 million; 33 percent reported sales of $51 million to $500 million; 7 percent were in the $501 million to $1 billion range; 10 percent had sales of $1.1 billion to $5 billion; and 6 percent had sales of over $5 billion.

CAPS wanted to see if transportation purchasing practices varied according to whether respondents reported data for their entire firm or only for their division or group. The responses were evenly split; of the 678 organizations, 340 (50.1 percent) submitted data for a division or group only, while 338 (49.9 percent) gave data for the entire firm.

Fig. 3—Small firms give buyers more transportation responsibility.

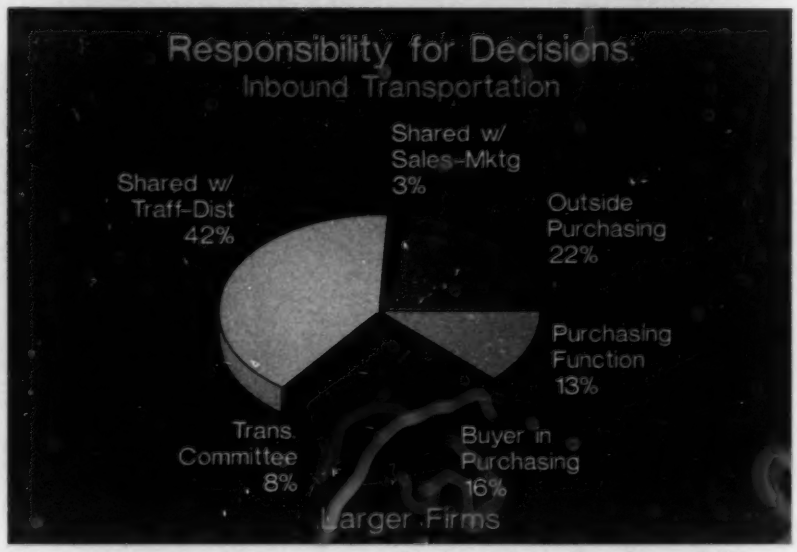

Fig. 4—Large companies are more likely to share the responsibility.

The results here are consistent with similar studies conducted for outbound transportation. Purchasing managers, like their counterparts in transportation, place greater emphasis on service factors than on cost. Because of technological advancements and marketing innovations, decisions on modes and carriers are far more complex today. Emphasizing service over cost makes it all the more important that these managers control inbound transportation and negotiate service standards with inbound carriers. As noted earlier, more and more managers are becoming involved in the carrier evaluation process to make sure these standards are met.

Organizational Relationships

Companies are organized in a number of ways to make inbound transportation decisions (Fig. 5, p. 42). The most common scenario, however, has purchasing sharing the decision-making responsibility with the traffic/distribution department (34 percent of the companies surveyed). In almost as many firms (27 percent), that responsibility rests solely with a buyer in the purchasing department. Other companies responded that the responsibility rests within purchasing but with someone other than a buyer (13 percent), while 15 percent said the responsibility rests outside purchasing altogether. In some companies the responsibility is shared by purchasing and sales/marketing, while others use a committee that includes purchasing, transportation and other departments.

Some interesting differences arise

continued

IN TRANSPORTATION DECISION MAKING, A LOT OF OLD BIASES STILL EXIST

DISTRIBUTION surveyed its readers to find out how *their* firms are organized to make transportation decisions. Our results were similar to CAPS'—with a notable exception. Only 15 percent of the CAPS respondents said responsibility for transportation decisions rests outside purchasing. In our survey, 31 percent said purchasing isn't involved (Fig. 6). Also, 27 percent of the CAPS respondents said such decisions were made by a buyer in purchasing. Only 9 percent of our readers said they're organized this way. Why the difference? CAPS surveyed a select number of purchasing managers; DISTRIBUTION readers hold a variety of purchasing and traffic/distribution titles. In fact, title is a good indicator of how a person will define purchasing's role in transportation:

• "Let traffic know what needs to be picked up. It's their job to bring the freight in." (distribution mgr.)

• "In most cases the traffic department is closer to the carrier community and what is happening in the transportation environment. In many cases, procurement personnel do not concern themselves with the cost of moving the goods." (traffic mgr.)

• "Transportation decisions are increasingly recognized as specialized purchasing decisions. The role of purchasing should increase." (dir. of materials)

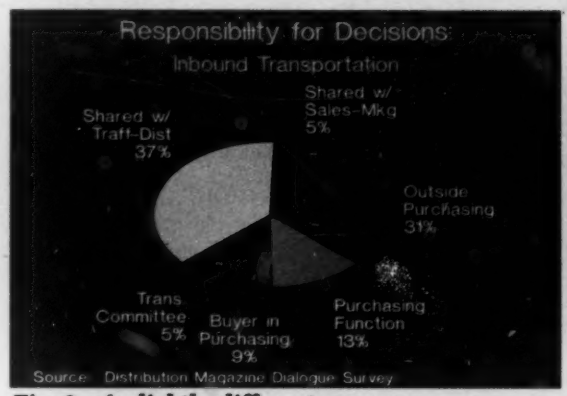

Fig. 6—A slightly different response.

• "Purchasing and traffic must be a shared role. Traffic employees should be aware of the negotiating skills that Purchasing uses and Purchasing must understand and use routing guides." (senior buyer)

• "Transportation and Purchasing both serve the company's prime function—having material available for manufacture or resale. Both must communicate with the goal of maximizing profit on sales, not just cutting costs." (distribution mgr.)

when the results for smaller and larger firms are compared (Fig. 3 & Fig. 4, p. 40). One conclusion, albeit a predictable one, is that larger firms are generally more likely to spread the responsibility for transportation decisions among several disciplines. These decisions are made entirely outside of the purchasing function in more larger firms than smaller ones. More larger firms share the responsibility with traffic/distribution, and twice as many larger firms use committees to make decisions. Smaller companies, on the other hand, are more likely to have a buyer within the purchasing department as the sole transportation decision maker.

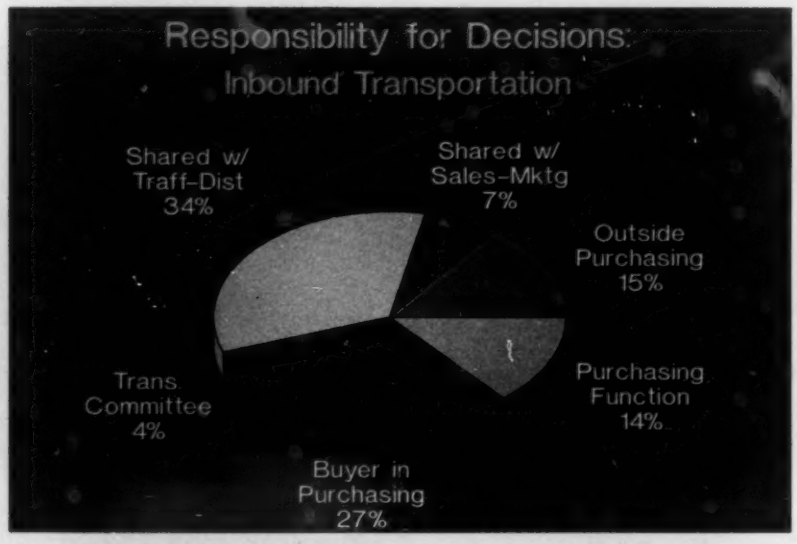

Fig. 5—It's important to assess buyers' transportation expertise.

Sharing the responsibility for transportation decisions enables companies to take advantage of the expertise found in purchasing *and* transportation. Those firms that leave the responsibility with a buyer need to assess the level of transportation knowledge possessed by that person. If a buyer is avoiding involvement in transportation by purchasing on a delivered price, opportunities for cost and service improvements may be slipping away.

Smaller firms tend to have a higher percentage of buyers making the transportation decisions, yet the data shows little variation in the percentage of FOB-Origin transactions versus FOB-Destination transactions by size of firms. This could indicate that buyers in small companies may, out of necessity, demonstrate more transportation expertise than buyers in large companies. ■